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COMTECH
GROUP INTERNATIONAL LIMITED

1973
ANNUAL
REPORT

COMTECH

Directors

Michel Bourbonnais
J. Heath Halliday
James E. Houston
Edward K. Loyst
Donald M. McPhail
John D. Morand
Sinclair M. Stevens

Officers

Sinclair M. Stevens, Chairman
Donald M. McPhail, President
J. Heath Halliday, Treasurer
Noreen M. Stevens, Secretary

Head Office

COMTECH GROUP INTERNATIONAL LIMITED
5 Fairview Mall Drive
Suite 450
Willowdale, Ont.
Area Code 416 - 492-1480

MONTREAL DATA CENTRE

COMTECH LIMITÉE
Suite 1000
9310 St. Laurent Blvd.
Montreal, Quebec
Area Code 514 - 382-3330

TORONTO DATA CENTRE

COMTECH GROUP LIMITED
5 Fairview Mall Drive
Suite 450
Willowdale, Ont.
Area Code 416 - 492-1480

AMERICAN OPERATIONS

COMTECH U.S.A. INC.
P.O. Box 784
Reston, Virginia, U.S.A.
Area Code 703 - 471-7141

Annual General Meeting

The 1973 Annual and General Meeting of Shareholders of Comtech Group International Limited will be held in the Prince Edward Island Room of the Royal York Hotel in Toronto, at 3:30 p.m. on September 25, 1973.

Highlights of Operations

	1973	1972
Total revenue	$1,509,342	$1,240,179
Package revenue	1,227,745	959,898
Costs and expenses	1,306,052	1,259,643
Net Income (loss)	206,741	(35,947)
Per common share		
Income (loss) before extraordinary items	.12	(.03)
Net Income (loss)	.25	(.05)
Average number of shares outstanding	830,772	758,752

TO OUR SHAREHOLDERS:

1973 has been a year of constructive achievement for the company. It has been a year of further growth in our product lines, of penetration of new market areas and of success financially.

FINANCIAL HIGHLIGHTS ARE:

1. Our income before taxes and extraordinary items was $203,290 compared to a loss of $19,464 in the previous year. Through continuing programs to increase our production efficiency, coupled with maximum effort to maintain a high degree of utilization of our resources, we have been able to absorb a 22% increase in our sales volume with no significant change (4%) in our total cost.

2. Our working capital position is now even compared to a working capital deficit of $197,000 the previous year. This change has been brought about primarily from funds generated through our profitability. In the coming year this trend in working capital will increase sharply as the central processor and some peripherals in our Toronto Centre are now paid for in full and the final payments on the balance of peripherals will be made in October 1973. This, coupled with further improvements in profitability, will continue to strengthen the company financially in the coming year.

3. Our long term debt has decreased from $370,606 to $73,304. This decrease is due to the conversion of a $200,000 debenture in January 1973 and the repayment of other forms of debt primarily related to our computer equipment.

With the further development of these financial trends toward a strong working capital position and the elimination of long term

debt, Comtech is developing a financial position that will prove advantageous in the coming years as the Canadian Computer Industry moves into a consolidating phase.

OPERATIONAL HIGHLIGHTS ARE:

1. Our new payroll product AUTOPAY and our ACCOUNTS RECEIVABLE product reached an annualized billing level of near $100,000 by the end of our year. This billing level reflects the market acceptance of our new products in the Toronto and Montreal areas. This market acceptance is more clearly seen in our internal operations with a steady inflow of new clients using these services.

In the coming year we expect this trend to accelerate as our General Ledger and Accounts Payable systems gain market acceptance.

2. Our licensing activities also showed marked growth in the latter part of the year. In February 1973 we entered into an agreement to make both our Canadian and U.S. Paymaster systems available on large scale I.B.M. equipment. Through this agreement we have obtained contracts for the processing of over 15,000 employees. These systems are now fully operational and we expect during the coming year to be processing payrolls on a remote job entry basis from Newfoundland to British Columbia.

In April through Comtech U.S.A. Inc. (of which we own 70% of the stock) we commenced a general marketing program in the U.S. for the licensing of our Paymaster. System. While this new program increased our cost levels in the latter part of the year, without a corresponding increase in revenue, we have seen an excellent acceptance of our systems and expect substantial income generation through this area in the coming year.

While our total licensing agreements have had little effect on improving our profitability in 1973, this area appears to have the greatest potential for rapid growth in the next five years. Software licensing has extremely high leverage and should provide substantial increases in the company's earnings in fiscal 1974 and future years.

3. In May the company relocated its Head Office and its Toronto Centre to new quarters at 5 Fairview Mall Drive. Our new facilities will provide for our anticipated expansion over the next five years and will allow Comtech to increase its activities in the area of client training.

Through our policies of specialization, Comtech has now emerged as the second largest independent payroll processor in North America and is the leading company in Canada. With further concentration of effort, we believe our Paymaster product will be one of the standard payroll systems in use throughout North America within the next five years.

On behalf of the Board of Directors

President

August 27, 1973

COMTECH's

Computer Package Accounting

...a package for growth

Today, Comtech is processing over 600 payrolls for large, medium and small companies and this continues to be the main thrust of the business. In 1970, Comtech predicted that it would become the number one supplier of payroll services in Canada. The company's successful marketing strategy is evidenced in this year's financial statement.

The software design team that made payroll such a winner developed and introduced additional accounting packages last year. With these additions, Comtech can now offer complete Computerized Package Accounting to Canadian business. With its added computing power capable to handling large-scale payrolls and its new policy by which large organizations as well as other data centres may use the Paymaster system under license, Comtech is confident of enhancing future profitability.

One of the first licenses to be granted for using Paymaster was issued at the end of 1971. The company is now ready to pursue this business in volume and has been actively marketing in this area since April of this year.

Here is a brief description of Comtech's product line of Computer Package Accounting systems.

Payroll services

Industry comparisons of payroll packages has placed Paymaster payroll system in the top spot in North America. It is at least equal to any other system on all points of comparison and superior in many of them. Added to this fact is that Paymaster is considerably less expensive than other comparable payroll systems.

Paymaster is an extremely sophisticated system geared to the employment patterns of the largest organizations with the most complex requirements. There are currently over 600 payrolls on Paymaster some of which service as many as 10,000 employees across Canada.

For smaller organizations and companies, with less complex payroll requirements, Comtech developed another package called Autopay. It is primarily designed for companies with 20 employees and upwards where fewer than 12 deductions are required. For a few cents a cheque, small companies can avail themselves of the benefits of a computerized system that takes care of all deductions, cumulative reports, UIC records and the year-end preparation of all T-4 slips.

Salaries and wages are in most cases the highest cost factors in business. Where these costs must be distributed to specific jobs, departments, burden centres or products, Comtech has developed a package to simplify the problem. The package is called Job Costing and dovetails with the payroll systems in order to distribute labour costs to the required cost centres. In addition, machines, materials and supplies can be distributed to provide up to the minute costs for comparison with budgets.

Since all information concerning each employee is included in his payroll file, Comtech developed a spinoff service for the personnel departments. From the computerized records, cards for the use of any department that may require them, are prepared. In some instances, complete sets may be kept in alphabetical order, in order of employee number, by seniority dates and so on.

Accounts receivable services

The Accounts Receivable package is one of the new accounting products introduced for the first time last year at the Canadian National Business Show. It is designed to speed up collections and cashflow, control credit limits, eliminate bookkeeping machines and specialized staff, ledger posting and statement preparation.

Customer invoice copies are picked up weekly, keypunched and returned with a batch listing for easy editing and a weekly aging of all accounts. Customer payments are recorded on a standard input form for easy entry into the computer. A copy of the same form is used as a deposit slip at the bank.

The customer receives a monthly sales journal detailing the customer number, invoice number, date, Federal and Provincial sales tax, discounts, freight charges and invoice amounts. He also receives a monthly aged trial balance on which each customer's credit limit is flagged. From this information the computer can provide a sales analysis showing such statistics as sales by salesman by product group, customer by product group, sales by territory by commission class and sales by salesman by customer. From these reports management can quickly pinpoint profitable areas of the business and spot potential markets.

General ledger and accounts payable services

The General Ledger and Accounts Payable packages are also new services introduced for the first time last year.

With the GL package, all receipts and disbursements are posted to an input sheet during the month. These sheets are collected and keypunched for input to the system which produces a General Ledger trial balance and Financial Statements along with fully detailed source journals.

The package has some special features such as provision for inserting budget figures, a full description of each accounting entry which is carried throughout the system, individual account analysis, a source and application of funds report and the ability to combine accounts automatically in up to three different ways. Consolidated statements from multiple levels of an organization with item descriptions from the lowest to the highest level, can be produced.

This package shortens month-end closing, provides budget comparisons, reduces the need for working papers by 75%, produces readjusted year-end statements and fully descriptive audit trials.

The Accounts Payable package provides the user with a systematic method of paying accounts by providing the immediate and accurate information needed to decide which vendors should be paid and when. The system gives complete and automatic distribution of all payments to their proper accounts.

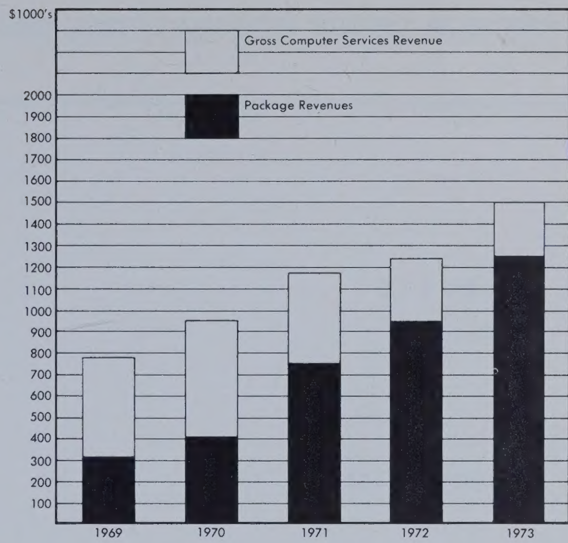
Licensing activities

Until recently Comtech's Paymaster payroll service has only been available through Comtech's data centre and paid for at so much per cheque depending on the number of employees on the payroll.

In 1972 Comtech negotiated its first American licensing agreement through which Paymaster payroll service is being offered in eastern United States cities. This has proved to be a profitable arrangement since it involves no equipment cash outlay or other overhead and immediately started generating royalty revenues for Comtech. During the last year, the U.S. centres using Paymaster have added $250,000 in new payroll business.

This year, Comtech has started actively promoting similar licensing arrangements in Canada to other data centres and also to large companies and organizations that wish to process their own payrolls. Where a company is spending more than $3,600 a year on payroll program maintenance, it can save money by using Paymaster.

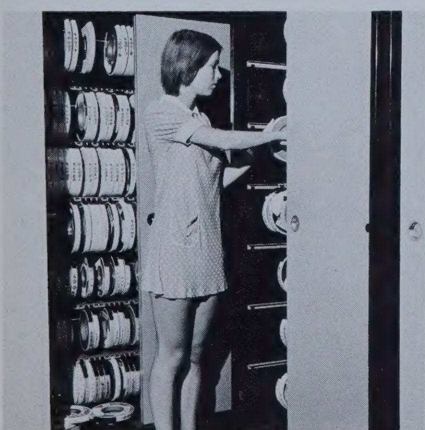
At present, over 40,000 people are being paid by companies and data centres using Paymaster under license. The expansion of licensing, both domestically and abroad, is expected to contribute a steady growth to company profits.

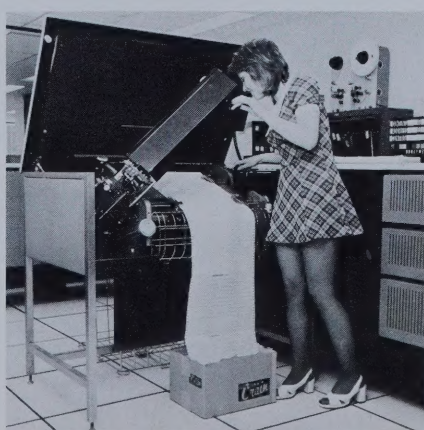


Head office and data centre...


Comtech's new head office location in Willowdale, Ontario.


Loading a tape in the data centre for a report run.


Client tapes are carefully stored under maximum security.


Special Comtech Report Forms used on this printer, are part of the total service.


Service Department checks input forms with client before data is entered into computer.

ASSETS

	1973	1972 (Note 1)
CURRENT ASSETS		
Cash	$ 34,739	$ 841
Accounts receivable	223,405	224,190
Inventories, at cost	27,998	13,674
Prepayments and advances	13,071	18,180
	299,213	256,885
FIXED ASSETS (Note 2)		
Cost	886,362	876,410
Accumulated depreciation	415,092	341,939
	471,270	534,471
PACKAGE PROGRAMMES (Note 3)	131,671	129,354
OTHER ASSETS AND DEFERRED CHARGES (Note 4)	20,666	27,693
EXCESS OF COST OF INVESTMENT IN SUBSIDIARIES OVER NET ASSETS ACQUIRED (Note 1)	595,729	601,809
	$1,518,549	$1,550,212

Signed on behalf of the Board:

Director

Director

Consolidated Balance Sheet as at June 30, 1973

LIABILITIES

	1973	1972 (Note 1)
CURRENT LIABILITIES		
Bank indebtedness	$ 45,000	$ 145,142
Accounts payable and accrued liabilities	160,947	181,360
Current maturities on long-term debt (Note 6)	97,301	126,544
	303,248	453,046
LONG-TERM DEBT (Note 6)	73,304	370,606
MINORITY INTEREST	4,536	1,310
	381,088	824,962

SHAREHOLDERS' EQUITY

	1973	1972
CAPITAL STOCK (Note 7)		
Authorized		
14,490 5% First preference shares $10 par value, cumulative, redeemable at $10.20 a share		
157,482 3% Second Preference shares $1 par value, non-cumulative, redeemable at par		
2,000,000 Common shares, $1 par value		
Issued		
4,490 5% Preference shares	44,900	44,900
55,482 3% Preference shares	55,482	55,482
872,463 Common shares	872,463	760,313
	972,845	860,695
CONTRIBUTED SURPLUS (Note 8)	93,320	—
RETAINED EARNINGS (Deficit) (Note 9)	71,296	(135,445)
	1,137,461	725,250
	$1,518,549	$1,550,212

Consolidated Statement of Income

FOR THE YEAR ENDED JUNE 30, 1973

	1973	1972
		(Note 1)
REVENUES		
Package processing and related services	$1,227,745	$ 959,898
Custom work and other	281,597	280,281
	1,509,342	1,240,179
COSTS AND EXPENSES		
Salaries and benefits	385,669	383,198
Computer operations	600,065	492,378
Marketing and administration	320,318	384,067
	1,306,052	1,259,643
Income (Loss) before taxes and extraordinary items	203,290	(19,464)
Provision for income taxes and minority interest		
Income taxes (Note 10)		
— Current	36,866	4,140
— Deferred	66,378	—
	103,244	4,140
Minority interest	3,339	1,320
	106,583	5,460
Income (Loss) before extraordinary items	96,707	(24,924)
Extraordinary items		
Tax recovery due to application of tax losses forward	100,348	10,975
Loss on disposal of customer list	—	(20,231)
Miscellaneous	9,686	(1,767)
	110,034	(11,023)
NET INCOME (LOSS)	206,741	(35,947)
EARNINGS PER SHARE		
Income (loss) before extraordinary items	.12	(.03)
Net income (loss)	.25	(.05)
Average number of shares outstanding	830,772	758,752

Consolidated Statement of Retained Earnings

FOR THE YEAR ENDED JUNE 30, 1973

	1973	1972
Retained Earnings (Deficit) at Start of Year	$(135,445)	$(216,555)
NET INCOME (LOSS)	206,741	(35,947)
	71,296	(252,502)
Transfer from contributed surplus (Note 9)	—	117,057
RETAINED EARNINGS (DEFICIT) AT END OF YEAR	$ 71,296	$(135,445)

Consolidated Statement of Source and Application of Funds

FOR THE YEAR ENDED JUNE 30, 1973

	1973	1972
SOURCE OF FUNDS		(Note 1)
Operations		
Net Income (Loss)	$ 206,741	$ (35,947)
Charges not requiring funds		
Depreciation on fixed assets	107,118	105,994
Loss on disposal of fixed assets	—	2,214
Amortization of deferred charges	47,474	38,815
Loss on disposal of customer list	—	20,231
Provision for deferred taxes and minority interest	675	(6,990)
	362,008	124,317
Issue of common shares for cash	12,510	3,150
Loan from the Industrial Development Bank	—	50,000
	$ 374,518	$ 177,467
APPLICATION OF FUNDS		
Purchase of fixed assets (net)	$ 43,917	$ 12,218
Package programme development costs	47,254	44,317
Retirement of long-term debt		
Notes on computer equipment	80,501	111,544
Other	16,800	15,000
Investment in shares of subsidiaries less working capital at dates of acquisition	(6,080)	13,488
Miscellaneous	—	3,006
	182,392	199,573
INCREASE (DECREASE) IN WORKING CAPITAL POSITION	192,126	(22,106)
	$ 374,518	$ 177,467

Auditors' Report

To the Shareholders of
Comtech Group International Limited

We have examined the consolidated balance sheet of Comtech Group International Limited and its subsidiaries as at June 30th, 1973 and the consolidated statements of income and retained earnings and source and application of funds for the year then ended. Our examination included a general review of the accounting procedures and such tests of accounting records and other supporting evidence as we considered necessary in the circumstances.

In our opinion, these consolidated financial statements present fairly the financial position of the companies as at June 30, 1973 and the results of their operations and source and application of their funds for the year then ended in accordance with generally accepted accounting principles applied on a basis consistent with that of the preceding year.

Toronto, Ontario,
August 20, 1973.

LAVENTHOL KREKSTEIN HORWATH & HORWATH,
Chartered Accountants.

Notes to 1973 Consolidated Financial Statements

1. **PRINCIPLES OF CONSOLIDATION**

The consolidated financial statements include the accounts of the following principal subsidiaries:

Name of Subsidiary	Date Acquired	Percentage Owned
Comtech Group Limited	June 3, 1969	100%
Subsidiaries of Comtech Group Limited		
Comtech (Central) Limited	March 30, 1968	100%
Comtech Limitée	August 7, 1968	100%
Commercial Computer Services Inc.	November 3, 1969	99.5%
Comtech New England Inc.	May 29, 1970	100%
Subsidiary of Comtech New England Inc.		
Comtech (U.S.A.) Inc.	Feb. 1, 1972	70%

On March 31, 1973 Comtech (Central) Limited was wound-up. The operations of this company have since been conducted by its parent, Comtech Group Limited and thus the excess of cost of investment in subsidiaries over net assets acquired amounting to $23,265 pertaining to Comtech (Central) Limited is still being carried.

The 1972 financial statements, presented for comparative purposes, have been reclassified to reflect consolidation of Comtech (U.S.A.) Inc., which had previously been recorded on the equity basis. This reclassification has no effect on consolidated net earnings as previously reported.

It is the company's policy not to amortize excess of cost of investment in subsidiaries over net assets acquired since management is of the opinion that there has been no diminution of value. However, certain items are treated as a recovery of part of the purchase price, where such items relate to events prior to the dates of acquisition. Such recoveries are credited to goodwill and in 1973 amounted to $6,080 ($8,200 in 1972 and $48,620 cumulative to date) composed primarily of income tax recoveries resulting from losses occurring prior to dates of acquisition.

2. **FIXED ASSETS**

	1973			1972
	Cost	Accumuated Depreciation	Net	Net
Computer equipment	$ 719,793	$ 329,993	$ 389,800	$ 469,509
Magnetic Tapes	35,392	26,077	9,315	14,247
Furniture and office equipment	94,234	49,917	44,317	48,337
Leasehold improvements	36,943	9,105	27,838	2,378
	$ 886,362	$ 415,092	$ 471,270	$ 534,471

The company depreciates its fixed assets on a straight-line basis over their estimated useful lives. Total depreciation during 1973 was $107,118 ($105,994 in 1972).

3. **PACKAGE PROGRAMMES**

	1973	1972
Balance at beginning of year	$ 129,354	$ 121,807
Package programme development costs capitalized during the year	47,254	44,317
	176,608	166,124
Amortization of package programmes	44,937	36,770
Balance at end of year	$ 131,671	$ 129,354

It is the company's policy to capitalize the costs of package programme development and to amortize such costs on a straight-line basis over a five-year period, commencing in the six month period following incurrance of the costs.

4. **OTHER ASSETS AND DEFERRED CHARGES**

	1973	1972
Deferred financing expense	$ —	$ 9,677
Deferred income taxes (Note 10)	19,050	16,500
Miscellaneous	1,616	1,516
	$ 20,666	$ 27,693

5. BANK INDEBTEDNESS

Accounts Receivable have been pledged as security for bank indebtedness.

6. LONG-TERM DEBT

	1973	1972
Lien notes payable on computer equipment (at interest approximating prime bank borrowing rates).		
Monthly principal of $2,122 to February 1973	$ —	$ 16,976
Monthly principal of $1,758 to October 1973	7,037	28,128
Monthly principal of $6,122 to March, 1975	128,568	202,046
	135,605	247,150
Convertible debentures payable		
7½% convertible, unsecured debentures to certain directors and senior officers	—	200,000
Loan payable		
9½% Secured loan payable to the Industrial Development Bank, $1,400 principal monthly to July 1975	35,000	50,000
	170,605	497,150
Less, current maturities	97,301	126,544
	$ 73,304	$ 370,606

During the year, all of the debentures were converted into 100,000 fully paid common shares at $2.00 per share.

The aggregate amounts of principal payments required for retirement provisions in each of the next five years are as follows:

1974	$ 97,301
1975	71,904
1976	1,400
1977	—
1978	—

The above amounts include the Industrial Development Bank loan based on contractual obligations. However, the company retired this loan in July, 1973.

7. SHARE CAPITAL

The company has an incentive stock option plan which provides for the issuance of five-year options to officers and key employees to purchase common shares at prices approximating market values at the dates of grants. These options become exercisable on a cumulative basis 20% per year. During the years ended June 30, 1973 and June 30, 1972 the following changes with respect to the plan occurred:

	1973	1972
Options outstanding at beginning of year	28,050	29,250
Options granted ($2.25 in 1972)	—	6,000
Options exercised ($1.00 to $1.40 in both years)	(12,150)	(2,950)
Options expired	(2,000)	(4,250)
Options outstanding at end of year	13,900	28,050

On the options outstanding at June 30, 1973 (7,050 until March 24, 1975, 850 until April 23, 1976 and 6,000 until March 22, 1977) the average option price was $1.56 per share. There are 2,200 shares available for future grants.

The increase in common share capital during the year is as follows:

	Number of shares	Par Value
Outstanding at beginning of year	760,313	$ 760,313
Conversion of 7½% debentures	100,000	100,000
Exercise of stock options	12,150	12,150
	872,463	$ 872,463

Dividends on the 5% cumulative preference shares have been paid to June 30, 1954. Arrears of dividends amount to $42,655 on the 4,490 shares outstanding. Since the company failed to pay more than three consecutive half-yearly dividends on the 5% cumulative preference shares and more than four consecutive

half-yearly dividends on the 3% non-cumulative preference shares, both classes of shares carry voting rights.

One of the subsidiary companies has unpaid cumulative preference dividends owing to minority shareholders in the amount of $5,906.

8. **CONTRIBUTED SURPLUS**

Balance at beginning of year	$ Nil
Premium received on common shares issued upon exercise of stock options	360
Excess of carrying value of debentures over par value of common shares issued on conversion	92,960
Balance at end of year	$ 93,320

9. **RETAINED EARNINGS**

During the years 1972 and 1971, transfers of $117,057 and $568,714 respectively were made from contributed surplus to reduce deficit.

10. **INCOME TAXES**

The company follows the tax allocation principle of providing for income taxes. Under this principle, a tax recovery debit of $2,550 ($16,500 in 1972) has been set up in respect of losses represented by unclaimed capital cost allowance, since in the opinion of management, it is virtually certain that future earnings will be sufficient to realize this amount.

At June 30, 1973 certain companies had accounting losses totalling $595,657 available to be carried forward for potential tax recoveries which have not been recognized in the accounts. Of this amount $322,475 consists of unclaimed capital cost allowances which can be carried forward indefinitely.

Accumulated losses which may be carried forward for income tax purposes are as follows:

Amount of tax loss	Available to
$ 42,796	1974
281,250	1975
97,759	1976
95,617	1977
5,973	1978
$ 523,395	

11. **COMMITMENTS**

The companies are committed to annual realty and equipment rentals of approximately $140,000 until 1977, $84,000 in 1978 and $23,000 thereafter until 1986.

12. **STATUTORY INFORMATION**

The aggregate direct remuneration paid or payable by the companies to the directors and senior officers of the company was $91,201 ($104,745 in 1972).

Total interest paid on long-term debt amounted to $19,936 ($48,175 in 1972).

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